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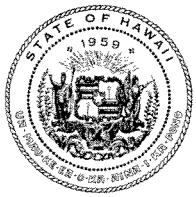
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



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March 3, 2010

[redacted text]

Re: General Excise Tax Exemption for Ship Repair of Federally Owned Vessels HRS § 237-28.1

Dear [redacted text]:

This responds to your request of [redacted text] for a ruling on Hawaii general excise tax liability for [redacted text] (the "Taxpayer"), the ship repair contractor hired by [redacted text] (the "Museum").

FACTS

Museum is a non-profit corporation and it is exempt from taxation pursuant to Internal Revenue Code section 501(c)(3). Museum's mission is to create and maintain a fitting memorial to the people and historic events reflecting our nation's proud legacy of duty, honor, strength, resolve and sacrifice. To accomplish its mission, Museum applied for and received [redacted text] (the "Vessel") under the Navy's Ship Donation Program for the purpose of operating a ship museum and memorial.

On [redacted text] the Department of Navy and Museum entered into [redacted text] (the "Contract"). The Vessel underwent a major dry dock repair as required under the Contract and Museum entered into a contract with the Taxpayer to do the ship repairs.

RULING REQUESTED

The requested ruling is that the Vessel is federally owned and therefore the Taxpayer will be exempt from general excise tax on proceeds received from Museum for repairs made on the Vessel pursuant to Hawaii Revised Statutes (HRS) section 237-28.1.

LAW AND ANALYSIS

HRS § 237-28.1 provides:

> There shall be exempted from, and excluded from the measure of, the taxes imposed by this chapter all of the gross proceeds arising from shipbuilding and ship repairs rendered to surface vessels federally owned or engaged in interstate or international trade.

A classic property law idiom holds that property ownership is akin to a bundle of sticks, with each stick representing a certain right to, or benefit of, that property. While Museum holds a few of the Vessel's "sticks," such as the right to use the Vessel in order to carry out its mission, in this case the majority of the "sticks" are still held by the federal government. For tax purposes, the Supreme Court has held that the owner of property is the person who has "actual command over the property taxed – the actual benefit for which the tax is paid."[1] As discussed below, according to the terms of the Contract, the Vessel is federally owned because the federal government retains the actual benefits and command of the property.

Pertinent terms and conditions from the Contract are below:

Under section No. 2, the Government has strict protocols on the movement of the Vessel, the maintenance and repair requirements, and areas that require Navy approval or the right to inspect; Museum cannot transfer or dispose of the Vessel or any part of the Vessel without the Navy's consent.

Under No. 4, Museum is required to maintain, at its own cost, certain types of insurance and at a stated minimum amount, but on some of the policies the Navy and/or the Government are named as the loss payee or as additional insured.

Under No. 8(a), the Navy during a national emergency has the unilateral right to request the immediate return of the Vessel including legal title without compensation.

Under No. 8(b), in the event there is a breach of the Contract which is not cured within a specified period of time, all rights to the Vessel are forfeited back to the Government including any improvements made by Museum that are attached to the Vessel.

Under No. 9, the Government retains the right to remove any equipment on the Vessel to meet the Navy's Fleet material needs without compensation, although the Navy will attempt to provide cosmetic pieces of equipment if the removed equipment affects the display of the Vessel.

Based on the terms and conditions of the Contract, the Government and/or the Navy has retained substantial rights in the Vessel and therefore there has not been complete transfer of the Vessel to Museum and in substance Museum only has a right to use the Vessel.

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[1] Grodt & McKay Realty, Inc. v. Commissioner of Internal Revenue, 77 T.C. 1221, 1236 (1981) (quoting Corliss v. Bowers, 281 U.S. 376, 378 (1930)).

In conclusion, the Vessel is in substance still federally owned based upon the terms of the Contract and therefore the Taxpayer will be exempt from general excise tax on proceeds received from Museum for repairs made on the Vessel pursuant to HRS § 237-28.1.

The conclusions reached in this letter are based on our understanding of the facts that Museum and the Taxpayer have represented. If it is later determined that our understanding of these facts is not correct, the facts are incomplete, or the facts later change in any material respect, the conclusion in this letter will be modified accordingly. This ruling also may be subject to change due to future amendments to laws, rules, or official Department positions.

If you have any further questions regarding this matter, please call me at 808-587-5334. Additional information on Hawaii's taxes is available at the Department's website at **www.state.hi.us/tax**.

Sincerely,

/s Jacob L. Herlitz

Jacob L. Herlitz
Administrative Rules Specialist

[redacted text]